

1

Student: _____

1. The balance sheet is made up of what five key components:

A.
B.
C.
D.
2. In terms of the balance sheet model of the firm, the value of the firm in financial markets is equal to:

A.
B.
C.
D.
E.
3. Inventory is a component of:

A.
B.
C.
D.
4. Using the balance sheet model of the firm, finance may be thought of as analysis of three primary subject areas. Which of the following groups correctly lists these three areas?

A.
B.
C.
D.
E.

5. Which of the following is not considered one of the basic questions of corporate finance?
- A.
 - B.
 - C.
 - D.
6. The need to manage net working capital arises because:
- A.
 - B.
 - C.
 - D.
 - E.
7. In the managerial structure of the corporation the two officers and their responsibilities that report directly to the Chief Financial Officer are:
- A.
 - B.
 - C.
 - D.
8. Value is created and recognized over time if:
- A.
 - B.
 - C.
 - D.
9. Time preference refers to the fact that:
- A.
 - B.
 - C.
 - D.

10. A corporate security can be viewed as a contingent claim on the firm. This means that:
- A.
 - B.
 - C.
 - D.
11. If a firm has debt outstanding the contingent claim of an equityholder is:
- A.
 - B.
 - C.
 - D.
12. The Simple Corporation has outstanding obligation to the Complex Corporation of \$250. It is year-end and the total cashflow of Simple from all sources is \$325. The contingent payoff to the debtholders and the equityholders is:
- A.
 - B.
 - C.
 - D.
13. The general partner(s) in a general partnership agree to share work, costs and profits and losses. Each partner:
- A.
 - B.
 - C.
 - D.
14. The division of profits and losses among the members of a partnership is formalized in the:
- A.
 - B.
 - C.
 - D.

15. The Splitz Corporation has borrowed \$5 million in debt with a promise to repay \$5.5 million in one year. The corporation had 10 million shares outstanding worth \$2 each at the time of the borrowing. Splitz earns \$6 million during the year. What is the debtholder's contingent claim; how much do the debtholders receive; and, how much do the equity holders receive.
- A.
B.
C.
D.
16. The Splitz Corporation has borrowed \$5 million in debt with a promise to repay \$5.5 million in one year. The corporation had 10 million shares outstanding worth \$2 each at the time of the borrowing. Splitz earns \$5 million during the year. What is the debtholder's contingent claim; how much does the debtholder receive; and, how much do the equity holders receive.
- A.
B.
C.
D.
17. Corporate securities are contingent claims because:
- A.
B.
C.
D.
18. Agency costs are the sum costs of:
- A.
B.
C.
D.

19. Agency costs refer to:
- A.
 - B.
 - C.
 - D.
 - E.
20. Managerial goals may differ from those of the shareholders. It is noted that managers may:
- A.
 - B.
 - C.
21. What is the primary goal of the corporation?
- A.
 - B.
 - C.
 - D.
22. Financial markets are composed of:
- A.
 - B.
 - C.
 - D.
23. The primary market is defined as:
- A.
 - B.
 - C.
 - D.
24. Which one of the following is a primary market transaction?
- A.
 - B.
 - C.
 - D.

25. Flea Fall Inc., a maker of dog flea collars, paid \$125,000 cash for inventory on January 1, 2010. On December 31, 2010, the company's sales total \$147,000 of which \$117,000 has been collected. If inventory represents Flea Falls only cost, calculate the firms accounting profit as well as its cash flow as of December 31.
26. The Harlow Corporation has promised to pay its debtholders an amount of \$2,700 over the next year. The firm's shareholders hold claim to whatever is left after the debtholders' claims have been satisfied. Calculate Harlow's debt and equity level if its assets total \$1100 at the end of the year. Recalculate for asset levels of \$2,200 and \$6,000.

27. A financial manager's most important job is to create value from capital budgeting, financing, and liquidity activities. Explain how financial managers create value.
28. The decision to incorporate must consider the fact that earnings will be taxed at both the corporate and personal levels. Since this is disadvantageous, provide three reasons why one may want to incorporate.
29. How can shareholders attempt to control managerial behavior to match shareholder interest?

30.

Do you think agency problems arise in sole proprietorships and/or partnerships?

1 Key

1. The balance sheet is made up of what five key components:

- A.
- B.
- C.**
- D.

Difficulty: Medium
Learning Objective: 01-01
Ross - Chapter 01 #1

2. In terms of the balance sheet model of the firm, the value of the firm in financial markets is equal to:

- A.
- B.
- C.
- D.**
- E.

Difficulty: Easy
Learning Objective: 01-01
Ross - Chapter 01 #2

3. Inventory is a component of:

- A.**
- B.
- C.
- D.

Difficulty: Easy
Learning Objective: 01-01
Ross - Chapter 01 #3

4. Using the balance sheet model of the firm, finance may be thought of as analysis of three primary subject areas. Which of the following groups correctly lists these three areas?

- A.
- B.
- C.
- D.
- E.

Difficulty: Easy
Learning Objective: 01-01
Ross - Chapter 01 #4

5. Which of the following is not considered one of the basic questions of corporate finance?

- A.
- B.
- C.
- D.

Difficulty: Easy
Learning Objective: 01-01
Ross - Chapter 01 #5

6. The need to manage net working capital arises because:

- A.
- B.
- C.
- D.
- E.

Difficulty: Easy
Learning Objective: 01-01
Ross - Chapter 01 #6

7. In the managerial structure of the corporation the two officers and their responsibilities that report directly to the Chief Financial Officer are:

- A.
- B.
- C.
- D.

Difficulty: Easy
Learning Objective: 01-01
Ross - Chapter 01 #7

8. Value is created and recognized over time if:

- A.
- B.
- C.**
- D.

Difficulty: Medium
Learning Objective: 01-01
Ross - Chapter 01 #8

9. Time preference refers to the fact that:

- A.
- B.
- C.**
- D.

Difficulty: Medium
Learning Objective: 01-01
Ross - Chapter 01 #9

10. A corporate security can be viewed as a contingent claim on the firm. This means that:

- A.**
- B.
- C.
- D.

Difficulty: Medium
Learning Objective: 01-02
Ross - Chapter 01 #10

11. If a firm has debt outstanding the contingent claim of an equityholder is:

- A.
- B.**
- C.
- D.

Difficulty: Medium
Learning Objective: 01-02
Ross - Chapter 01 #11

12. The Simple Corporation has outstanding obligation to the Complex Corporation of \$250. It is year-end and the total cashflow of Simple from all sources is \$325. The contingent payoff to the debtholders and the equityholders is:

- A.
- B.
- C.**
- D.

Difficulty: Medium
Learning Objective: 01-02
Ross - Chapter 01 #12

13. The general partner(s) in a general partnership agree to share work, costs and profits and losses. Each partner:

- A.
- B.**
- C.
- D.

Difficulty: Medium
Learning Objective: 01-03
Ross - Chapter 01 #13

14. The division of profits and losses among the members of a partnership is formalized in the:

- A.
- B.
- C.
- D.**

Difficulty: Easy
Learning Objective: 01-03
Ross - Chapter 01 #14

15. The Splitz Corporation has borrowed \$5 million in debt with a promise to repay \$5.5 million in one year. The corporation had 10 million shares outstanding worth \$2 each at the time of the borrowing. Splitz earns \$6 million during the year. What is the debtholder's contingent claim; how much do the debtholders receive; and, how much do the equity holders receive.

- A.
- B.
- C.
- D.**

Difficulty: Medium
Learning Objective: 01-03
Ross - Chapter 01 #15

16. The Splitz Corporation has borrowed \$5 million in debt with a promise to repay \$5.5 million in one year. The corporation had 10 million shares outstanding worth \$2 each at the time of the borrowing. Splitz earns \$5 million during the year. What is the debtholder's contingent claim; how much does the debtholder receive; and, how much do the equity holders receive.

- A.
- B.**
- C.
- D.

Difficulty: Medium
Learning Objective: 01-03
Ross - Chapter 01 #16

17. Corporate securities are contingent claims because:

- A.
- B.
- C.**
- D.

Difficulty: Hard
Learning Objective: 01-03
Ross - Chapter 01 #17

18.

Agency costs as the sum costs of:

- A.
- B.**
- C.
- D.

Difficulty: Hard
Learning Objective: 01-04
Ross - Chapter 01 #18

19.

Agency costs refer to:

- A.
- B.
- C.
- D.**
- E.

Difficulty: Easy
Learning Objective: 01-04
Ross - Chapter 01 #19

20.

Managerial goals may differ from those of the shareholders. It is noted that managers may:

- A.
- B.
- C.**

Difficulty: Hard
Learning Objective: 01-04
Ross - Chapter 01 #20

21.

What is the primary goal of the corporation?

- A.
- B.**
- C.
- D.

Difficulty: Easy
Learning Objective: 01-04
Ross - Chapter 01 #21

22. Financial markets are composed of:

- A.
- B.
- C.**
- D.

Difficulty: Easy
Learning Objective: 01-05
Ross - Chapter 01 #22

23. The primary market is defined as:

- A.
- B.**
- C.
- D.

Difficulty: Easy
Learning Objective: 01-05
Ross - Chapter 01 #23

24. Which one of the following is a primary market transaction?

- A.
- B.**
- C.
- D.

Difficulty: Medium
Learning Objective: 01-05
Ross - Chapter 01 #24

25. Flea Fall Inc., a maker of dog flea collars, paid \$125,000 cash for inventory on January 1, 2010. On December 31, 2010, the company's sales total \$147,000 of which \$117,000 has been collected. If inventory represents Flea Falls only cost, calculate the firms accounting profit as well as its cash flow as of December 31.

Accounting Profit = Sales - Cost (\$147,000 - \$125,000 = \$22,000
Cash Flow = Cash Inflow-Cash Outflow (\$117,000 - \$125,000 =(\$8,000)

Difficulty: Medium
Learning Objective: 01-01
Ross - Chapter 01 #25

26.

The Harlow Corporation has promised to pay its debtholders an amount of \$2,700 over the next year. The firm's shareholders hold claim to whatever is left after the debtholders' claims have been satisfied. Calculate Harlow's debt and equity level if its assets total \$1100 at the end of the year. Recalculate for asset levels of \$2,200 and \$6,000.

If assets total \$1100: Value of Debt = \$1100, Value of Equity = \$0

If assets total \$2200: Value of Debt = \$2200, Value of Equity = \$0

If assets total \$6000: Value of Debt = \$2700, Value of Equity = \$3300

Difficulty: Medium
Learning Objective: 01-01
Ross - Chapter 01 #26

27.

A financial manager's most important job is to create value from capital budgeting, financing, and liquidity activities. Explain how financial managers create value.

Buy assets that generate more than their cost.

Sell financial securities that raise more cash than they cost.

Minimize cash payouts to non-investors, ie., taxes to governments.

Difficulty: Medium
Learning Objective: 01-01
Ross - Chapter 01 #27

28. The decision to incorporate must consider the fact that earnings will be taxed at both the corporate and personal levels. Since this is disadvantageous, provide three reasons why one may want to incorporate.

Easier access to capital markets.
Retention of funds for reinvestment opportunities.
Market pricing and trading of securities.

Difficulty: Hard
Learning Objective: 01-03
Ross - Chapter 01 #28

29. How can shareholders attempt to control managerial behavior to match shareholder interest?

Vote for directors with shareholder's interest to select management.
Provide incentive contracts; performance shares or options.
Outside threat of takeover, (Board should not be willing to launch poison pills.)
Managerial labor market.

Difficulty: Hard
Learning Objective: 01-04
Ross - Chapter 01 #29

30. Do you think agency problems arise in sole proprietorships and/or partnerships?

Agency conflicts typically arise when there is a separation of ownership and management of a business. In a sole proprietorship and a small partnership, such separation is not likely to exist to the degree it does in a corporation. However, there is still potential for agency conflicts. For example, as employees are hired to represent the firm, there is once again a separation of ownership and management.

Difficulty: Hard
Learning Objective: 01-04

1 Summary